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# Supreme Court of the United States

OCTOBER TERM, 1957.

No. 368

IDEAL MERCANTILE CORPORATION,
Petitioner,

—vs.—

GALLANT FABRICS, INC., etc.
(Petitioning Creditors).

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**PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT.**

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erential transfer (Appendix to Appellant's Brief, pp. 20-23). The said order of the District Court adjudged the assignment of the customs refund claims was not a legal assignment but an equitable assignment and an act of bankruptcy by reason whereof it adjudged Ideal Mercantile Corporation a bankrupt.

## Opinions Below

The opinion of the United States Court of Appeals for the Second Circuit is not yet officially reported (Appendix A).

The opinion of the District Court is officially reported at 143 F. Supp. 810 (Appendix to Appellant's Brief, pp. 27-36).

The opinion of the Referee in Bankruptcy is not officially reported (Appendix to Appellant's Brief, pp. 20-23).

## Jurisdiction

The decree of the United States Court of Appeals for the Second Circuit, sought to be reviewed, was filed on June 21, 1957 (Appendix B).

The jurisdiction of this Court is invoked under 28 U. S. C. 1254. See, also, § 24a of the Bankruptcy Act (11 U. S. C. 47(a)).

## Questions Presented

The questions presented for review are:

(1) Are customs refund claims assignable?

(2) Was the assignment of a customs refund claim a legal assignment, valid as between the parties?

(3) Did the assignment of the customs refund claim on August 2, 1954 (Appendix to Appellant's Brief, pp. 39-42) under the laws of the State of New York which required nothing further to be done to perfect a legal assignment, constitute an act of bankruptcy as alleged in the involuntary petition in bankruptcy filed on February 11, 1955?

## Statutes Involved

Section 3(a)(2) (11 U. S. C. A. § 21(a)(2)) of the Bankruptcy Act, in so far as is relevant, provides:

> "(a) Acts of bankruptcy by a person shall consist of his having * * * (2) made or suffered a preferential transfer, as defined in subdivision a of section 60 of this Act."

The pertinent provisions of the Bankruptcy Act, § 60(a)(1) (11 U. S. C. 96(a)(1)), in so far as is relevant, provides:

> "A preference is a transfer * * * of any of the property of a debtor to or for the benefit of a creditor for or on account of an antecedent debt, made or suffered by such debtor while insolvent and within four months before the filing by or against him of the petition initiating a proceeding under this title, the effect of which transfer will be to enable such creditor to obtain a greater percentage of his debt than some other creditor of the same class."

Section 60(a)(2), 11 U. S. C. 96(a)(2), in so far as is relevant, provides:

> "For the purposes of subdivision (2) and (b) of this section, a transfer of property other than real property shall be deemed to have been made or suffered at the time when it became so far perfected that no subsequent lien upon such property obtainable by legal or equitable proceedings on a simple contract could become superior to the rights of the transferee * * * if any transfer of other (than real) property is not so perfected against such liens by legal or equitable proceedings prior to the filing of a petition initiating a proceeding under this title, it shall be deemed to have been made immediately before the filing of the petition."

31 U. S. C. A. 203, in so far as is relevant, provides:

> "All transfers and assignments made of any claim upon the United States, or of any part or share thereof, or interest therein, whether absolute or conditional, and whatever may be the consideration therefor, and all powers of attorney, orders, or other authorities for receiving payment of any such claim, or of any part or share thereof, except as hereinafter provided, shall be absolutely null and void, unless they are freely made and executed in the presence of at least two attesting witnesses, after the allowance of such a claim, the ascertainment of the amount due, and the issuing of a warrant for the payment thereof * * *."

## Statement of Case

The facts with respect to the issues on this petition are not in dispute.

On November 19, 1954, an involuntary petition in bankruptcy was filed against Ideal Mercantile Corporation, the petitioner herein. The petition alleged acts of bankruptcy in general terms and upon a motion to dismiss the same the petitioning creditors were granted leave to file an amended petition.

The amended petition was filed on February 11, 1955 enumerating new acts of bankruptcy, including one specific act charging the execution and delivery on August 2, 1954, by Ideal Mercantile Corporation to Kraditor & Haber, of an assignment of all of its claims for refund duties paid under protest to the United States, which assignment is claimed to constitute a preferential transfer.

An answer was interposed to the amended petition and the Referee, after a trial of the issues, which centered about the assignment of the claim for customs refunds, made findings of fact and conclusions of law and handed down an opinion (Appendix to Appellant's Brief, pp. 20-23) dismiss-

ing all of the acts of bankruptcy as not proved nor established, except the act charging that the delivery of an execution to the Sheriff on December 31, 1954 created a lien on the property of Ideal Mercantile Corporation.

The Referee found and held that the assignment of the customs refund duties, under the laws of the State of New York, was completed upon delivery, with nothing more remaining to make it effective and was not required to be filed nor recorded, and having taken place more than four months prior to the filing of the petition on February 11, 1955, did not constitute an act of bankruptcy (Appendix to Appellant's Brief, p. 23).

Upon review, District Judge Edward Weinfeld found that the execution delivered to the Sheriff on December 31, 1954, did not create a lien on the property of Ideal Mercantile Corporation and did not constitute an act of bankruptcy, but did find that the assignment of the customs refund was not a legal assignment, but an equitable assignment, which was not perfected at the time of the filing of the petition on February 11, 1955, by reason of which it constituted an act of bankruptcy and adjudged Ideal Mercantile Corporation a bankrupt (Appendix to Appellant's Brief, pp. 27-36).

Both the District Court and the Court of Appeals held that the assignment of the customs refund claim would not constitute a preference and would not be an act of bankruptcy if it was "perfected" on August 2, 1954.

On appeal, the United States Court of Appeals held that the assignment was "absolutely null and void" when made on August 2, 1954, even as between the parties, that the assignment was not perfected within the meaning of the Bankruptcy Act (11 U. S. C. A. 96 (a) (2)), and deemed the assignment made immediately before the filing of the amended petition and an act of bankruptcy.

This matter presents three conflicting opinions—(1) that of the Referee holding the assignment of customs refund claims to be a valid legal assignment as between the parties, perfected on execution and delivery; (2) that of the District

Court holding the assignment a valid assignment as between the parties but an equitable assignment which was not perfected at the time of the filing of the petition in bankruptcy; and (3) that of the United States Court of Appeals holding the assignment to be null and void as between the parties and deemed to have been made immediately before the filing of the amended petition.

## Reasons For Granting The Writ

The decision of the United States Court of Appeals is in conflict with the decisions of the Supreme Court of the United States, other Circuits and District Courts and prior decisions within the Second Circuit.

The questions raised are of vital importance to the business world generally as well as in the administration of the Bankruptcy Act.

With respect to the business world the question is of vital importance as to the status of refund claims, whether for customs duties or income taxes, and whether such claims are to be immobilized pending the allowance of the claim by the issuance of warrants, or whether they may be utilized by way of assignments, either absolute or as security in connection with business and financing transactions, without in any wise affecting the rights of the Government.

In so far as the administration of the Bankruptcy Act is concerned the question is of extreme importance in view of the conflict of opinions between the various Circuits, within the Second Circuit as well as with the decisions of the Supreme Court.

The decision of the Court below is inconsistent and in conflict with the decisions of this Court in *Martin* v. *National Surety Co.*, 300 U. S. 588, and *McKenzie* v. *Irving Trust Company*, 323 U. S. 365, whereunder this Court recognized and held that assignments of refund claims were valid as between the parties and as against a trustee in bankruptcy.

Even Judge Weinfeld in the decision in the District Court recognized and held that the assignment of the customs refund claims was valid as between the parties.

In *Martin* v. *National Surety Co., supra,* this Court said:

> "The provisions of the statute making void an assignment or power of attorney by a Government contractor are for the protection of the Government."
>
> * * * * *
>
> "A transfer of the fund after payment is perfected is of no concern to any one except the parties to the transaction and this quite irrespective of the time of the assignment or the manner of its making."

In *McKenzie* v. *Irving Trust Co., supra,* this Court, by Mr. Chief Justice Stone, in referring to 31 U. S. § 203, said:

> "The provisions of the statute governing assignments of claims against the Government are for the protection of the Government and not for the regulation of the equities of the claimants as between themselves. Martin v. National Surety Co., 300 U. S. 588, 594, 595."

As to what constitutes a transfer and when it is completed under § 60(2), the Court said:

> "In the absence of any controlling Federal Statute, a creditor or bona fide purchaser could acquire rights in the property transferred by the debtor, only by virtue of a state law. And hence § 60, sub. a's 'apparent' command is to test the effectiveness of a transfer, as against the trustee, by the standards which applicable state law would enforce against a good-faith purchase.' Corn Exchange Nat. Bank & Trust Co. v. Klauder, 318 U. S. 434, 436, 437, 63 S. Ct. 679, 681, 87 L. Ed. 884, 144 A. L. R. 1189. See also Benedict v. Ratner, 268 U. S. 353, 359, 45 S. Ct. 566, 567, 69 L. Ed. 991, and cases cited. Section 60, sub. a in this respect, as do numerous other federal statutes, see Davies Warehouse Co. v. Bowles, 321 U. S. 144, 155, 156, 64 S. Ct. 474, 480, 481, and note 20, and cases cited, thus adopts state law as the rule of de-

cision. "The state standards which control the effectiveness of a transfer likewise determine the precise time when a transfer is deemed to have been made or perfected."

The cases of *Martin* v. *National Surety Company* and *McKenzie* v. *Irving Trust Company, supra,* have been construed by other courts to lay down the rule that an assignment of a claim against the Government is valid as between the parties notwithstanding the fact that such an assignment does not comply with the provisions of 31 U. S. C. § 203; that a claim for refund of customs duties or income taxes is property which may be the subject of a legal assignment perfected on execution and delivery of the assignment.

*Bank of California* v. *Commissioner of Internal Revenue,* (C. A. 9) 133 F. 2d 428;

*California Bank* v. *U. S. Fidelity & Guaranty Co.,* (C. A. 9) 129 F. 2d 751;

*In re Webber Motor Co.,* (D. C. N. J.) 52 F. Supp. 742;

*In re Italian Cook Oil Corporation,* (C. A. 3) 190 F. 2d 994;

*In re Gerstenzang,* (S. D. N. Y.) 5 F. Supp. 904;

*Erwin* v. *U. S.,* 97 U. S. 392;

*Harlan* v. *Archer,* (C. A. 4) 79 F. 2d 673;

*U. S.* v. *Certain Lands in Town of Highlands, New York,* (S. D. N. Y.) 49 F. Supp. 962;

*Roomberg* v. *U. S.,* (D. C. Pa.) 40 F. Supp. 621.

Assignments of claim against the United States, even before their allowance, are valid as between the parties, notwithstanding 31 U. S. C. § 203.

*Bank of California* v. *Commissioner of Internal Revenue,* (C. A. 9) 133 F. 2d 428;

*California Bank* v. *U. S. Fidelity & Guaranty Co.*, (C. A. 9) 129 F. 2d 751;

*In re Webber Motor Co.*; 52 F. Supp. 742.

The failure to comply with the Federal Assignment of Claims statute is immaterial to the decision of this case. If the assignment is valid under State Law it is valid as against the trustee. Under the laws of the State of New York, the assignment of the refund claims was valid and perfected on execution and delivery, which took place on August 2, 1954, more than four months prior to the filing of the petition and hence it cannot constitute an act of bankruptcy.

*Rockmore* v. *Lehman*, (C. A. 2) 129 F. 2d 893, cert. den. 317 U. S. 700;

New York Personal Property Law § 41;

*Scarborough* v. *Berkshire Fine Spinning Asso.*, (S. D. N. Y.) 128 F. Supp. 948, 951, 952;

*M. M. Landy, Inc.* v. *Nicholas*, (C. A. 5) 221 F. 2d 923.

Even the Courts of the State of New York have held an assignment of a claim against the Government to be valid as between the parties, notwithstanding the Federal Assignment of Claims Act.

*Sterling* v. *Miller*, 2 App. Div. 2d 900;

*Coastal Commercial* v. *Central Bank of Yonkers*, 119 N. Y. Supp. 2d 857.

The decisions cited by the District Court are not applicable and misconstrue the *nature of a refund* claim. The District Judge based his decision on *In re Modell*, (C. A. 2) 71 F. 2d 148, involving an assignment by a bankrupt of its right to a recovery in a malicious prosecution action prior to the recovery of a judgment, which under the laws of the State of New York is not assignable.

The District Court also relied on *In re Silver Cup Bar & Grill, Inc.*, (S. D. N. Y.) 50 F. Supp. 528, involving an assignment of a refund on a liquor license where the assignor remained in possession of the license and did not surrender the license until one week prior to the filing of the involuntary petition and some ten months after the assignment. The right to a refund in this case, did not come into being until one week before the filing of the petition and until the license was surrendered.

This is a vastly different situation from the case at bar. Here, claims for refund were in existence, constant, fixed and unaffected by lapse of time. The claims were in the same category as any claim arising on a contract or to recover the excess payment made in error with the right of collection merely in dispute, but unaffected by lapse of time.

If permitted to stand, the decision below will immobilize, as a business asset, tax refunds, whether for income taxes or customs duties. This would have a disastrous effect both as a tax matter as well as from a business and economic standpoint.

Tax refunds run into the hundreds of millions of dollars annually. If these cannot be availed of for business purposes, to be used in the course of conduct of business as between the parties, without in any wise prejudicing the rights of the Government, it would have a serious and adverse effect on business and unnecessarily restrict the flow of credit and the use of actual assets in the conduct of business. Tax refunds can readily be utilized in the conduct of business, either as security for loans or by outright sale and transfer of the same, subject, however, at all times, to the paramount and prior rights of the Government.

Furthermore, the decision of the Court below is in direct conflict with the decisions of this Court in *Martin* v. *National Surety Co.* (*supra*) and *McKenzie* v. *Irving Trust Co.* (*supra*) and is in direct conflict with the Ninth Circuit and other Courts with respect to the interpretation of the decisions of this Court, the validity of an assignment as between the parties and its status as a legal assignment as against a trustee.

## CONCLUSION

Petitioner respectfully submits that the conflict between the Second Circuit and the Ninth Circuit as well as other Circuits and District Courts (*In re Webber*, 52 F. Supp. 742) with respect to the interpretation of the decisions of this Court and the validity of the assignment of the refund claim as between the parties and its status as a legal assignment, the conflict of opinions within the Second Circuit and that of the various District Courts, and the importance of the issues, both as a tax and business problem as well as one involving the Bankruptcy Act, should be resolved in the interest of uniform and orderly administration of law with respect to controversies arising out of bankruptcy proceedings and involving tax, business and economic problems and controversies.

WHEREFORE, your petitioner prays that a writ of certiorari issue under the seal of this Court, directed to the United States Court of Appeals for the Second Circuit, commanding the said Court to certify and send to this Court a full and complete transcript of the record and of the proceedings of the said Court of Appeals had in this case to the end that this cause may be reviewed and determined by this Court, as provided for by the statutes of the United States; and that the judgment herein of said Court of Appeals for the Second Circuit be reversed by this Court, and for such further relief as to this Court may seem proper.

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## APPENDIX A

# UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT.

No. 163—October Term, 1956.

(Argued January 24, 1957—Decided May 20, 1957)

Docket No. 24298.

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IN THE MATTER OF

IDEAL MERCANTILE CORPORATION,

Bankrupt,

IDEAL MERCANTILE CORPORATION,

Appellant.

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Before: HINCKS, LUMBARD and WATERMAN, Circuit Judges.

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Appellant, having been petitioned into involuntary bankruptcy, sought review of order of Referee adjudging it bankrupt. Upon review by U. S. District Court for the Southern District of New York, Weinfeld, J., decision of Referee was upheld. Upon appeal, decision below, 143 F. Supp. 810, affirmed.

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SCHWARTZ, RUDIN & DUBERSTEIN (MAX SCHWARTZ on the brief), Brooklyn, New York, for Appellant.

FREDA SILBOWITZ (MICHAEL BERMAN on the brief), New York City, for Petitioning Creditors.

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WATERMAN, Circuit Judge:

The appellant, the Ideal Mercantile Corporation, appeals from an order of the District Court reversing in part an

order of the Referee in this bankruptcy proceeding. The Referee had found, insofar as his findings are relevant to the disposition of this appeal, that an assignment by Ideal of certain customs refund claims was not a preferential transfer made within four months prior to the filing of an amended involuntary petition in bankruptcy. The District Court rejected this finding, and held that the assignment constituted an act of bankruptcy under the relevant provision of the Bankruptcy Act, 11 U. S. C. A. § 21(a)(2),[1] and by reason thereof adjudged Ideal a bankrupt.

The Ideal Mercantile Corporation was organized in August 1950, and was thereafter engaged in the business of importing and manufacturing china and ladies' ready to wear clothing. The Company was insolvent on and after July 20, 1954, and it ceased doing business in August of that year. On August 2, 1954, Ideal executed and delivered to the firm of Kraditor and Haber, its attorneys and accountants, an assignment of all its claims for the refund of customs duties paid under protest to the United States. The duties were paid on scarves imported from Japan. The claims aggregated $38,447.85, and were assigned in full payment of an antecedent indebtedness of $11,491.09 allegedly due to the assignees from Ideal for accounting and legal services and a loan of approximately $2500.00. At the time of the assignment and at the time of the filing of the amended petition in bankruptcy, these claims had not been allowed by the

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[1] "(a) Acts of bankruptcy by a person shall consist of his * * * (2) made or suffered a preferential transfer, as defined in subdivision a of section 96 of this title * * *" 11 U. S. C. A. § 21(a)(2).

Insofar as here relevant, 11 U. S. C. A. § 96(a) provides:

"(1) a preference is a transfer * * * of any of the property of a debtor to or for the benefit of a creditor for or on account of an antecedent debt, made or suffered by such debtor while insolvent and within four months before the filing by or against him of the petition initiating a proceeding under this title, the effect of which transfer will be to enable such creditor to obtain a greater percentage of his debt than some other creditor of the same class."

United States, but were being prosecuted on behalf of the assignor.

On November 19, 1954, three creditors of Ideal filed an involuntary petition in bankruptcy against Ideal. The petition alleged in general terms the making of fraudulent and preferential transfers, but it did not specify dates, amounts, or transferees. Upon Ideal's motion to dismiss the petition for indefiniteness, the petitioning creditors cross-moved for, and were granted, leave to serve an amended petition. The amended petition was filed on February 11, 1955, enumerating specific acts of bankruptcy.

The assignment of the customs refund claims was first discovered by the petitioning creditors during an examination of an officer of Ideal conducted on December 28, 1954, under the original petition. Therefore the District Court sustained the Referee's finding that the petitioning creditors, when they filed the orginal petition on November 19, 1954, neither knew of, nor attempted to plead, the assignment. Accordingly, the assignment was properly regarded as a newly alleged act of bankruptcy, and was not related back to the date of the original petition for the purpose of determining whether it was preferential. *Dworsky* v. *Alanjay Bias Binding Corp.*, 182 F. 2d 802 (2d Cir. 1950); *cf. Glint Factors, Inc.* v. *Schnapp*, 126 F. 2d 207 (2d Cir. 1942).

Throughout this litigation the assignment of the customs refund claims has been attacked by the petitioning creditors as preferential. But, as noted by the District Court, the assignment would not constitute a preference, and hence would not be an act of bankruptcy, if it was "perfected" on August 2, 1954, when it was made, because that date was more than four months before the filing of the amended petition. 11 U. S. C. A. §§ 21(a)(2), 96(a)(1).

When the assignment was made on August 2, 1954, it was "absolutely null and void" as against the Government under the Assignment of Claims Act because the customs refund claims had never been allowed by the United States and no warrant had been issued for their payment. 31 U. S. C. A.

§ 203.[2] The judge below pointed out, however, that the bar against assignment of claims against the United States is "for the protection of the Government and not for the regulation of the equities of the claimants as between themselves," 143 F. Supp. at 813, citing *McKenzie* v. *Irving Trust Co.*, 323 U. S. 365, 369 (1945), and *Goodman* v. *Niblack*, 102 U. S. 556, 560 (1881). Thereupon he reasoned that the Assignment of Claims Act had no effect upon the validity or enforceability of an assignment of a claim against the United States as between the parties to that assignment or their successors in interest. The District Court then held that under the applicable state law, that of New York, the assignment was not perfected within the meaning of the Bankruptcy Act at the time of its making on August 2, 1954, and therefore it must be deemed to have been made immediately before the filing of the amended petition. 11 U. S. C. A. § 96(a)(2).[3] Accordingly, the Court held that the assignment, which was made when Ideal was insolvent, was a preferential transfer and hence an act of bankruptcy.

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[2] Insofar as here relevant, 31 U. S. C. A. § 203 provides:

"All transfers and assignments made of any claim upon the United States, or of any part or share thereof, or interest therein, whether absolute or conditional, and whatever may be the consideration therefor, and all powers of attorney, orders, or other authorities for receiving payment of any such claim, or of any part or share thereof, except as hereinafter provided, shall be absolutely null and void, unless they are freely made and executed in the presence of at least two attesting witnesses, after the allowance of such a claim, the ascertainment of the amount due, and the issuing of a warrant for the payment thereof * * *."

[3] Insofar as here relevant, 11 U. S. C. A. § 96(a)(2) provides:

"For the purposes of subdivision (a) and (b) of this section, a transfer of property other than real property shall be deemed to have been made or suffered at the time when it became so far perfected that no subsequent lien upon such property obtainable by legal or equitable proceedings on a simple contract could become superior to the rights of the transferee * * * if any transfer of other (than real) property is not so perfected against such liens by legal or equitable proceedings prior to the filing of a petition initiating a proceeding under this title, it shall be deemed to have been made immediately before the filing of the petition."

We affirm the District Court in its ultimate conclusion that the assignment of the custom refunds claims constituted an act of bankruptcy, but we reach that conclusion by a different course of reasoning from that of the District Court.

The point at which a transfer is perfected within the meaning of the Bankruptcy Act is generally determined by reference to the applicable state law, here the law of New York. *In re Morasco*, 233 F. 2d 11, 13 (2d Cir. 1956); see 3 Collier, Bankruptcy Para. 60.39 (14th ed. 1956) and cases there collected. But in making that determination where the transfer is an alleged assignment of a claim against the United States, a New York court will first take in consideration the effect, if any, of the federal Assignment of Claims Act. See, *e.g.*, *McKenzie* v. *Irving Trust Co.*, 292 N. Y. 347, 55 N. E. 2d 192 (1944), aff'd, 323 U. S. 365 (1945); *Rodd* v. *Kamen Products Co.*, 275 App. Div. 855, 89 N. Y. S. 2d 406 (2d Dep't 1949).

The Assignment of Claims Act was first enacted in 1853, purportedly (1) "to prevent persons of influence from buying up claims against the United States, which might then be improperly urged upon officers of the Government," (2) "to prevent possible multiple payment of claims, to make unnecessary the investigation of alleged assignments, and to enable the Government to deal only with the original claimant," and (3) "to save to the United States 'defenses which it has to claims by an assignor by way of set-off, counterclaim, etc., which might not be applicable to an assignee.'" *United States* v. *Shannon*, 342 U. S. 288, 291-92 (1952); see *United States* v. *Aetna Surety Co.*, 338 U. S. 366, 373 (1949); *Goodman* v. *Niblack*, 102 U. S. 556, 560 (1880); *Spofford* v. *Kirk*, 97 U. S. 484, 490 (1878).

In *National Bank of Commerce* v. *Downie*, 218 U. S. 345 (1910), the Supreme Court held that the assignment of unpaid and unallowed claims against the United States was void as against the subsequent trustee in bankruptcy of the assignor. The Court did not rest its decision on the ground

that the claims had not been paid or even allowed at the time of the filing of the petition in bankruptcy, but held the purported assignment to be "absolutely null and void, and as not, in itself, passing to the appellants (creditor-assignees) any interest, present or remote, legal or equitable, in the claims transferred." *National Bank of Commerce* v. *Downie, supra*, at 356.

Subsequently, however, in the case of *Martin* v. *National Surety Co.*, 300 U. S. 588 (1937), the Supreme Court held that a conditional assignment by a contractor to his surety of payments due on a government contract, although not made in compliance with the Assignment of Claims Act, was enforceable against one who, with notice of the prior assignment, had loaned money to the contractor-assignor and, under power of attorney from the contractor, had collected the deferred payments from the Government and applied them to his loan. Pointing out that the Assignment of Claims Act was enacted for the protection of the Government, Mr. Justice Cardozo, speaking for the Court, stated that "the Government is not concerned to regulate the equities of claimants growing out of irregular assignments *when collection is complete and liability is ended* * * * A transfer of the fund *after payment is perfected* is of no concern to any one except the parties to the transaction, and this quite irrespective of the time of the assignment or the manner of its making." *Martin* v. *National Surety Co., supra*, at 595. (Emphasis added.)

Thus, without overruling the *Downie* decision, the Supreme Court in *Martin* v. *National Surety Co.* limited the prior decision to assignments of unpaid claims against the Government, declaring that "after payments have been collected and are in the hands of the contractor or subsequent payees with notice, assignments (previously made) may be heeded, at all events in equity, if they will not frustrate the ends to which the prohibition was directed." *Martin* v. *National Surety Co., supra*, at 596-97.

The *Martin* case has been cited subsequently by the Supreme Court, and it seems clear that an assignment of a

claim against the United States is enforceable in many cases as between the parties to that assignment, or their successors in interest, after the Government has paid the claim. *McKenzie v. Irving Trust Co.*, 323 U. S. 365, 369 (1945); *cf. Central Bank v. United States*, 345 U. S. 234, 237 n. 1 (1947); see Note, 12 A. L. R. 2d 460, 468-75 (1950) and cases there collected.

Here the customs refund claims had not even been allowed, much less paid, at the time of the filing of the amended petition in bankruptcy on February 11, 1955. At that date the assignment of those claims was unenforceable between the parties, and therefore could not be considered "perfected" within the meaning of the Bankruptcy Act, 11 U. S. C. A. § 96(a)(2). Hence the assignment must be deemed to have been made immediately before the filing of the amended petition, 11 U. S. C. A. § 96(a)(2); and, accordingly, it constituted an act of bankruptcy, 11 U. S. C. A. § 21(a)(2).

Several other contentions were urged in this appeal but it is unnecessary to consider them in view of our finding that the assignment of the customs refund claims was a preferential transfer.

Order affirmed.

APPENDIX B

# UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT.

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At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the 20th day of May, one thousand nine hundred and fifty-seven.

Present: HON. CARROLL C. HINCKS,
HON. J. EDWARD LUMBARD,
HON. STERRY R. WATERMAN,
*Circuit Judges.*

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IN RE IDEAL MERCANTILE CORP.,
Bankrupt,

IDEAL MERCANTILE CORPORATION,
Appellant,

JACK EBER, *et al.*,
Appellees.

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Appeal from the United States District Court for the Southern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York, and was argued by counsel.

IN CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the order of said District Court be and it hereby is affirmed, with costs to the appellee.

A. DANIEL FUSARO,
Clerk.

Office - Supreme Court, U.S.
FILED
SEP 11 1957
JOHN T. FEY, Clerk

# Supreme Court of the United States

OCTOBER TERM, 1957—No. 368

IDEAL MERCANTILE CORPORATION,

Petitioner,

*against*

GALLANT FABRICS CO., INC., Etc.

(Petitioning Creditors)

## BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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# Supreme Court of the United States

OCTOBER TERM, 1957—No. 368

IDEAL MERCANTILE CORPORATION,

Petitioner,

*against*

GALLANT FABRICS CO., INC., etc.
(Petitioning Creditors)

## BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

### Reasons for Denying the Writ

This brief is submitted on behalf of the petitioning creditors, in opposition to the petition of Ideal Mercantile Corporation, for a writ of certiorari to the United States Court of Appeals for the Second Circuit.

The petitioner has based its application for a writ of certiorari upon the following grounds:

(a) The decision of the United States Court of Appeals is in conflict with the decisions of the Supreme Court of the United States, other Circuits and District Courts and prior decisions within the Second Circuit.

(b) The questions raised are of vital importance to the business world generally, as well as in the administration of the Bankruptcy Act.

It shall be shown, hereinafter, that there is no conflict in the decisions, and that the business world will not be adversely affected by the decision of the Court of Appeals.

The cases in this Court have consistently followed the rule of law promulgated in the case of *National Bank of Commerce* v. *Downie,* 218 U. S. 345, 31 S. Ct. 89, 54 L. Ed. 165, where the Court held that a transfer of a claim against the United States is absolutely void, and said as follows:

> "They are clean-cut cases of a voluntary transfer of claims against the United States, before their allowance, in direct opposition to the statute. If any regard whatever is to be had to the intention of Congress, as manifested by its words—to clear, we think to need construction—we must hold such a transfer to be absolutely null and void, and as not, in itself, passing to the appellants any interest, present or remote, legal or equitable, in the claims transferred."

It should be noted that the claims which were assigned had not yet been paid by the United States and although the decision is not based on that fact, it is important to note for a complete understanding of the decisions which follow. The decision of the Supreme Court in this case was followed in a number of cases. Matter of *Guarantee Title & Trust Company,* 185 Fed. 373 affg. on rearg. 193 Fed. 52; *Hudford Co. of New York* (C.C.A. 2d Cir.), 257 Fed. 722. This decision was also followed by the Court of Appeals of the State of New York in the case of *Manhattan Commercial Co.* v. *Paul,* 216 N. Y. 481, 111 N. E. 76.

Approximately thirty years later this court again interpreted Section 203, Title 31, U.S.C.A., in the case of *Martin* v. *National Surety Co.,* 300 U. S. 588, 57 S. Ct. 531, 81 L. Ed. 822. The facts in this case were entirely different from the facts in the case of *National Bank of Commerce* v. *Downie, supra.* In this case a contractor had made an assignment of claims which it had against the government

to a surety who had posted a bond for performance of this work. The assignment was given to the surety to protect materialmen and others who performed services and furnished materials on this job. Subsequent to the execution and delivery of this assignment the contractor gave a power of attorney to Martin to collect the moneys owing from the government which was given as security for moneys advanced by Martin. Martin took the power of attorney with knowledge of the prior assignment to the surety. *The litigation arose after the government had made payment of the moneys owing to the contractor, to Martin.*

The court pointed out that since the moneys had already been paid by the government, it no longer was concerned with the validity or invalidity of the assignment. The court did not expressly or impliedly overrule its decision in the case of *National Bank of Commerce against Downie, supra.* It merely pointed out that since the statute was enacted for the benefit of the government, the government no longer had any concern with the matter once it had paid out the moneys. It pointed out that as between the parties to the assignment, there might arise an equitable claim *after the moneys had come into the possession of the assignor.* The court said as follows, at page 597:

> "After payments have been collected and are in the hands of the contractor or subsequent payee with notice, assignments may be heeded, at all events in equity, if they will not frustrate the ends to which the prohibition was directed. See Lay v. Lay, 248 U. S. 24 affg. 118 Miss. 549; 79 So. 291. * * * *An assignment ineffective at law may none the less amount to the creation of an equitable lien when the matter of the assignment has been reduced to possession and is in the hands of the assignor or of persons claiming under him with notice.* (Citing cases)" (Italics mine.)

The Court distinguished *National Bank of Commerce* v. *Downie, supra,* at page 596:

> "Thus in National Bank of Commerce v. Downie, supra, to give a single illustration, where the controversy was between the trustee in bankruptcy of the contractor and prior assignees, the claims against the Government which were the subject of the assignment had never been allowed, much less collected, although the decision cannot be said to have been put on that ground."

The next case that came before this Court was *McKenzie* v. *The Irving Trust Company,* 323 U. S. 365, 65 S. Ct. 405. The decision of this Court in this case was based entirely upon its finding that payment had been made four months prior to the filing of the petition in bankruptcy and therefore no preference had been created. The assignment in this case was made to a bank and therefore came within the exception contained in the statute, except that the bank had failed to comply with the formalities provided for in the statute. Mr. Justice Lehman in a decision rendered by the Court of Appeals of the State of New York in the same case, 292 N. Y. 347, 353, said as follows:

> "The assignment delivered by the bankrupt on November 22, 1940 would undoubtedly have been 'absolutely null and void' if the statute had not been amended on October 9, 1940 for the express purpose of authorizing, subject to conditions therein specified, the assignment of claims against the United States arising even under contracts theretofore made with the Government."

It is important to note that in *McKenzie* v. *Irving Trust Company, supra,* the litigation arose *after payment had been made by the Government.* The Court said at page 369:

> "Here, the payment having been made to the contractor and by it delivered to respondent before the

assignment was perfected, the Government's obligation was discharged; and the situation was no different than it would have been if no assignment had been made."

In the case of *M. M. Landy Inc.* v. *Nicholas*, 221 F. (2) 923, the litigation arose after warrants had been issued, the Court said as follows:

"The cases of National Bank of Commerce of Seattle v. Downie, 218 U. S. 345, 31 S. Ct. 89, 54 L. Ed. 1065 and Spoffard v. Kirk, 97 U. S. 484, 24 L. Ed. 1032, which said that such an assignment was of no effect and unenforceable even between the parties thereto, have never been expressly overruled, although Martin v. National Surety Company, 300 U. S. 588, 57 S. Ct. 531, 81 L. Ed. 822, distinguishing Downie on the ground that there payment had not been made by the Government at the time the assignee sought to enforce the assignment, reached a result quite inconsistent with the *ratio dicidendi* in Downie." * * * *.

In a case decided in the Supreme Court of the State of New York where payment had not been made by the Government, the Court held the assignment void. In the case of *Rodd* v. *Kamen Products Co. Inc.*, 275 App. Div. 855, 89 N. Y. Supp. 2d 406, the Court said as follows:

"The assignment delivered to plaintiff was void. Manhattan Commercial Co. v. Paul, 216 N. Y. 481, 111 N. E. 76; Martin v. National Surety Co., 300 U. S. 588, 57 S. Ct. 531, 81 L. Ed. 822; McKenzie v. Irving Trust Co., 292 N. Y. 347, 55 N. E. 2d 192. It was not executed in accordance with Federal Law. U. S. Code, Tit. 31 Sec. 203, 31 U.S.C.A. Sec. 203, U. S. Rev. Stat. Sec. 3477. No warrant for payment had issued and payment thereunder had not been made. The United States was a creditor of the corporation. The assignment had no present value and, therefore, could not

work a discharge of the notes. Wise v. Chase, 44 N. Y. 337, 340. At best it was a conditional payment of the notes. Cherey v. McLaughlin, 245 N. Y. 616, 157 N. E. 881. It would become effective only if and when the United States issued its warrant and made payment of the over-assessment of income taxes. * * *"

The rationale of the cases cited seems to be, that as between the parties to an assignment of a claim against the Government; the validity or invalidity thereof will depend upon whether the claim against the Government were allowed and paid at the time the litigation arose or even as indicated in the New York decisions cited above, at the time of the decision. An assignment of a claim against the Government which has not been allowed, its amount ascertained and a warrant issued for its payment passes nothing to the assignee. It is not until the amount of the claim has been ascertained, allowed by the Government and a warrant issued for its payment that the Courts have held that some rights were transferred by the assignment whether they be legal or equitable.

The decision of the United States Court of Appeals in this case is in accord with the prior decisions of this court, of the United States Court of Appeals for the Second Circuit and of the decisions in other circuits.

The petitioner has cited the cases of the *Bank of California* v. *Commissioner of Internal Revenue* (C. A. 9) F. 2d 428, and the *California Bank* v. *The U. S. Fidelity & Guaranty Co.* (C. A. 9) 129 F. 2d 751, as being in conflict with the decision of the United States Court of Appeals in this case.

The case of the *Bank of California* v. *Commissioner of Internal Revenue, supra,* involved the question of fixing the value of a claim for the refund of taxes paid by a decedent. The question involved, was, whether this claim should be valued for estate tax purposes, prior to its

allowance. The estate contended that since the claim was not assignable by virtue of Section 203, Title 31, U.S.C.A., it had no value for tax purposes. The Court held, that regardless of the assignability or lack of assignability of this claim it had a value for estate tax purposes. In deciding this case, the Court stated the general rule, that Section 203, Title 31, U.S.C.A. was enacted for the benefit of the Government. This decision is not in conflict with the decision of the United States Court of Appeals in this case.

The case of *California Bank* v. *U. S. Fidelity & Guaranty Co., supra,* involved the question of the equities between an assignee of a claim against the Government and a creditor of the claimant who received payment from the claimant without knowledge of the prior assignment. The Court held that the creditor was entitled to retain the monies that it had received since it had received the same without notice of the prior assignment.

It should be noted that this case involved the rights of the parties *after* the monies had been paid out by the Government. This case is not in conflict with the decision of the United States Court of Appeals in this case.

Judge Weinfeld in his decision in the District Court rightly compared an assignment of claim which had not been allowed, to an assignment of a liquor license refund. In the so-called "liquor license cases" the Courts of New York have held that the assignment of a refund due on a liquor license transfers nothing, until the license has been surrendered and the fund has come into existence. It has been held in these cases that an intervening creditor who levies upon the refund is superior to the rights of the assignee even though the assignment was made prior thereto. See, *Atlas Advertising Agency, Inc.* v. *The Casa Cubana Inc.*, 259 App. Div. 951, 19 N.Y.S. 2d 900; *Aecher Realty Corp.* v. *Meredith Restaurant, Inc.*, 256 App. Div. 853, 8 N. Y. 2d 733. See also, *In Re Silver Cup Bar & Grill Inc.*, S.D.N.Y. 50 F. Supp. 528.

In an assignment of a claim against the Government there is no fund in existence nor is there anything to assign until, as directed by the statute, "after the allowance of such a claim, the ascertainment of the amount due, and the issue of a warrant for the payment thereof".

The assignment which was made by the bankrupt in this case to Kraditor and Haber on August 2, 1954 was an assignment of a fund not in existence. At the time of the filing of the amended petition in bankruptcy and up to the present time, this fund has not yet come into existence. It has not been ascertained, allowed or a warrant issued for its payment.

This assignment was therefore not perfected at the time of the filing of the amended petition in bankruptcy and therefore is deemed to have been perfected immediately prior thereto and within four months of the filing thereof.

Section 3 of the Bankruptcy Act provides:

> "a. Acts of bankruptcy by a person shall consist of his having * * * (2) made or suffered a preferential transfer as defined in subdivision a of Section 60 of this Act * * *.
>
> "b. A petition may be filed against a person within four months after the commission of an act of bankruptcy. * * * and such time with respect to the second act of bankruptcy shall not expire until four months after the date when the transfer became perfected as prescribed in subdivision a of Section 60 of this Act."

Section 60a(2) defines perfection of transfer as follows:

> "For the purposes of subdivisions a and b of this section, a transfer of property other than real property shall be deemed to have been made or suffered at the time when it became so far perfected that no subsequent lien upon such property obtainable by legal or

equitable proceedings on a single contract could become superior to the rights of the transferee. * * * if any transfer * * * is not so perfected against such liens by legal or equitable proceedings prior to the filing of a petition initiating a proceeding under this Act, it shall be deemed to have been made immediately before filing of the petition."

The determination of when the assignment was perfected defends upon state law. *In Re Morasco*, 2 Cir. 233 F. 2d 11, 13.

The cases decided in the State of New York hold that an assignment of a fund not yet in existence creates an equitable assignment but if the fund should come into existence within four months prior to the filing of the petition in bankruptcy, the right of the assignee would be subordinate to the rights of creditors.

*In re Modell*, 2 Cir., 71 F. 2d 148;
*Titusville Iron Co.* v. *City of New York*, 207 N. Y. 203;
*Zartman* v. *First National Bank of Waterloo*, 189 N. Y. 267;
*Atlas Advertising Agency, Inc.* v. *Casa Cubana, Inc.*, 259 App. Div. 951, 19 N.Y.S. 2d 900;
*Okin* v. *Isaac Goldman Co.*, 79 F. 2d 317 (C.C.A. 2).

The assignment made when the bankrupt was concededly insolvent, and not perfected up to the time of the filing of the amended petition, constitutes a preferential transfer within four months and an act of bankruptcy.

The petitioner raises the question of the importance of this issue to the business world and intimates that if the decision of the Circuit Court of Appeals is sustained it will vitally affect business transactions. The statute forbidding the assignment of claims against the Government 31

U.S.C.A. 203, contains an exception to its general rule forbidding the assignment of claims. That exception provides as follows:

> "The provisions of the preceding paragraph shall not apply in any case in which the monies due or to become due from the United States or from any agency or department thereof, under a contract providing for payments aggregating $1,000 or more, are assigned to a bank, trust company, or other financing institution, including any Federal lending agency: provided . . ."

The business world will therefore not be affected by the decision in this case, since a claimant with a claim against the Government may freely assign and borrow money thereon by transacting his business with a bank, trust company or other financing institution.

## Conclusion

The decision of the United States Court of Appeals for the Second Circuit is not in conflict with any decisions in the Second Circuit, the Ninth Circuit or any other Circuits or District Courts, nor is it in conflict with the decisions of this Court.

The business world will not be affected by the decision in this case since the holder of a claim against the United States may assign and transfer the same to a bank and trust company or other financing institution in accordance with the provisions of Section 203, Title 31, U.S.C.A.

WHEREFORE, it is respectfully submitted that the application made by the petitioner for a writ of certiorari to the United States Court of Appeals for the Second Circuit, be denied.

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